

Message Text

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ACTION EUR-12

INFO OCT-01 IO-13 ISO-00 SP-02 ICA-11 AID-05 EB-08
NSC-05 TRSE-00 SS-15 STR-07 OMB-01 CEA-01 CIAE-00
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R 221422Z MAY 78
FM AMEMBASSY LISBON
TO SECSTATE WASHDC 5788
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
USMISSION GENEVA
AMEMBASSY LONDON
AMEMBASSY MADRID
AMEMBASSY PARIS

C O N F I D E N T I A L LISBON 3780

PARRIS ALSO FOR OECD; BRUSSELS FOR USEC; DEPT PASS TREASURY FOR
SYVRUD; DEPT PASS EXIMBANK FOR ALBRIGHT

E.O. 11652: GDS
TAGS: ECON EFIN PO
SUBJ: IMF AGREEMENT: LETTER OF INTENT: COMMENT

REF: LISBON 3754

1. CONCLUSION OF GOP/IMF AGREEMENT, PUBLICLY SYMBOLIZED BY
LETTER OF INTENT, HAS CONTRIBUTED SIGNIFICANTLY TO IMPROVING
FOREIGN BANKING SYSTEM'S ATTITUDE TOWARD PORTUGAL. THIS IM-
PRESSION CAME THROUGH CLEARLY DURING PRIVATE EMBASSY DIS-
CUSSIONS OF PAST FEW DAYS WITH BANK OF PORTUGAL (BOP) OFFICIALS
AND WITH AMERICAN BANKERS. BOP OFFICERS HAVE VIRTUALLY CON-
CLUDED NEGOTIATIONS FOR PRIVATE GERMAN BANK PARTICIPATION IN
THE COORDINATED INTERNATIONAL LENDING PROGRAM. FINAL AGREEMENT
DELAYED APPARENTLY ONLY BECAUSE GERMAN BANKERS ARE SEEK-
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ING TO OVERSUBSCRIBE PREVIOUSLY ANNOUNCED \$200 MILLION
GERMAN PARTICIPATION. BOP IS EXPLOITING THIS FACTOR TO
THE MAXIMUM. IT HAS ADVISED SEVERAL BANKS THAT, IF THEY
WISH TO PARTICIPATE IN THE \$200 MILLION LOAN, THEY MUST
PROVIDE ADDITIONAL LONG-TERM FINANCING OUTSIDE THE COORDI-
NATED LENDING PROGRAM FRAMEWORK. SEVERAL GERMAN BANKS HAVE
REPORTEDLY PROPOSED PACKAGE ARRANGEMENTS INCLUDING BOTH

THEIR PARTICIPATION IN THE \$200 MILLION LOAN AND ADDITIONAL SUBSTANTIAL SEVEN YEAR CREDITS. BOP HOPES TO CONCLUDE THESE AGREEMENTS PROMPTLY AND TO USE THE TERMS OBTAINED THEREIN AS A BENCHMARK (READ LEVERAGE) IN DISCUSSIONS WITH AMERICAN BANKERS. BOP FEELS VIRTUALLY CERTAIN THAT IT CAN OBTAIN SOME SEVEN-YEAR MONEY FROM U.S. BANKS. IT MAY, HOWEVER, ASK AMERICAN BANKS FOR FIVE-YEAR TERMS, THEREBY HOPING TO MAXIMIZE THE SIZE OF THE LOAN PACKAGE.

2. KEY GOP ECONOMIC OFFICIALS APPARENTLY HAVE DECIDED ALREADY TO ENTER MULTI-YEAR THIRD AND FOURTH CREDIT TRANCHE NEGOTIATIONS WITH THE FUND LATER THIS YEAR. MINISTER OF FINANCE CONSTANCIO VIRTUALLY ADMITTED AS MUCH DURING HIS NATIONWIDE TV PRESENTATION FRIDAY, MAY 19. HIS PRIVATE COMMENTS EARLIER IN THE DAY TO EMBASSY OFFICER SUGGESTED THAT HE WOULD BE PREPARED TO ENTER SUCH NEGOTIATIONS WHEN THE FIRST EFFECTS OF THE RECENT EXCHANGE AND CREDIT POLICY INNOVATIONS BECOME APPARENT. PRESUMABLY HE HAS AN OCTOBER OF NOVEMBER DATE IN MIND.

3. FOLLOWING ARE COMMENTS ON SPECIFIC POINTS IN THE LETTER OF INTENT:

A. DRAWDOWN: DRAWDOWN OF THE SECOND TRANCHE WILL BE PHASED OVER THE PROGRAM YEAR, WITH A SLIGHTLY LARGER PORTION DRAWN DURING THE EARLY PHASE. EMBASSY PRESUMES THAT EFFECTIVE DRAWDOWN WILL BE APPROXIMATELY \$55 MILLION IN CY 1978
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AND \$15 MILLION IN CY 1979.

B. GDP: GOP PROJECTION OF A 27 PERCENT NOMINAL GROWTH IN GDP INDICATES THAT IT ANTICIPATES NO REAL GROWTH THIS YEAR. IN FACT, IT MAY EVEN ANTICIPATE A SLIGHT DECLINE.

C. CREDIT CEILING: BOP HAS ALREADY GIVEN INDIVIDUAL COMMERCIAL BANKS THEIR MANDATORY CREDIT CEILINGS. ALTHOUGH BOP HAS REQUESTED THAT THE BANKS INSTITUTE MEASURES TO INSURE THE AVAILABILITY OF CREDIT TO BOTH PRIVATE AND PUBLIC SECTOR ENTERPRISES, THIS ISSUE IS CAUSING CONSIDERABLE PROBLEMS. THE BANKS, IN EFFECT, HAVE NO DESIRE TO EXTEND ADDITIONAL CREDIT TO MOST PUBLIC SECTOR ENTERPRISES, BUT THEY ARE UNDER CONSIDERABLE PRESSURE TO DO SO.

D. SHORT-TERM CREDIT: PORTUGAL'S PLEDGE TO AVOID AN INCREASE IN PRIVATE SHORT-TERM FOREIGN DEBT WILL BE FEASIBLE ONLY IF GOP SUCCEEDS IN OBTAINING CONSIDERABLE MEDIUM AND LONG-TERM FINANCING AND/OR IT TRANSFORMS SUBSTANTIAL AMOUNTS OF EXISTING SHORT-TERM DEBT INTO LONGER-TERM OBLIGATIONS.

4. THE LETTER OF INTENT CONTAINS SEVERAL STATEMENTS OF GOP WILLINGNESS TO ADAPT ITS POLICIES TO FUTURE ECONOMIC DEVELOPMENTS. EMBASSY BELIEVES ADDITIONAL BUDGETARY AND/

OR CREDIT MEASURES WILL LIKELY BE REQUIRED OVER THE COMING
MONTHS. GOP'S FLEXIBILITY IN RECOGNIZING THIS NEED AND IN
ACTING PROMPTLY WILL PROBABLY BE DECISIVE FOR THE
STABILIZATION PROGRAM'S SUCCESS.
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